TRADEWINDS PROPERTIES SDN BHD v. ZULHKIPLE A BAKAR & ORS

COURT OF APPEAL, PUTRAJAYA
MOHD ZAWAWI SALLEH JCA
VERNON ONG LAM KIAT JCA
HASNAH MOHAMMED HASHIM JCA
[CIVIL APPEAL NO: W-02(NCVC)(W)-1734-08-2017]
12 SEPTEMBER 2018

COMPANY LAW: *Fraudulent trading – Intent to defraud – Allegation of – Action commenced against first defendant as director and second defendant company in a suit – Default on terms of payment – Breach of consent judgment – Incorporation of third defendant company by first defendant due to suit – Whether equated to fraudulent trading – Whether third defendant company incorporated prior to consent judgment in contemplation of evading payments – Whether there was clear intention of defendants attempting to defraud plaintiff by depriving it from receiving sums agreed in consent judgment – Companies Act 1965, s. 304(1), (2)*

COMPANY LAW: *Lifting of corporate veil – Mala fide actions – Action commenced against first defendant as director and second defendant company in a suit – Incorporation of third defendant company by first defendant due to suit – Whether third defendant company incorporated to receive payments of fees for work undertaken by second defendant company – Whether second defendant company's expenses borne by third defendant company – Whether both companies operated as single commercial entity – Whether first defendant alter ego of both companies – Whether corporate veil ought to be lifted*

The appellant ('the plaintiff') commenced an action against the first respondent ('first defendant') and second respondent ('second defendant') ('suit 93'). At the material time, the first defendant was one of two directors and held 100% shareholding in the second defendant company. A consent judgment ('CJ') was entered between the parties. Pursuant to the CJ, the plaintiff, together with the first and second defendants, agreed to settle Suit 93. The material terms of the CJ were, *inter alia*, (i) that the first and second defendants pay RM1,150,000 to the plaintiff as full and final settlement ('settlement sum'); (ii) that the settlement sum was to be paid by instalments; (iii) in the event of a default on the terms of payment, the plaintiff must first issue a notice to the first defendant and/or second defendant giving a five month period to remedy the default ('five month notice'); and (iv) in the event the first defendant and/or second defendant still failed to remedy the default, the plaintiff could execute the CJ for the sum of RM1,450,000 ('full judgment sum'). The first defendant and/or the second defendant paid a total of RM654,000 in accordance with the terms of the CJ and towards satisfaction of the settlement sum. Subsequently, the second

defendant breached the CJ when it failed to pay the instalments for the months of March 2013 to June 2013 as prescribed under the CJ. To this end, the plaintiff issued the five month notices in respect of each of these breaches, all of which expired without any of the default being remedied. The full judgment sum remained outstanding and due to the plaintiff. The plaintiff then became aware of three consultancy projects that the second defendant was engaged with PLB-KH Bina Sdn Bhd, Tech-Art Sdn Bhd and Putrajaya Holdings Sdn Bhd ('the three projects'). The second defendant passed three resolutions ('the resolutions') to reassign the consultancy fees due to the second defendant for the three projects to the third respondent company ('third defendant'), which was incorporated by the first defendant. The plaintiff contended that the resolutions were made to defraud the plaintiff, as a creditor of the payment of the balance sum due under the terms of the CJ. The plaintiff initiated an action against the first defendant, second defendant and third defendant seeking, *inter alia*, a declaration that the first defendant had carried on the business of the second defendant with the intention to defraud the plaintiff, as the second defendant's creditor. The High Court, in finding that the plaintiff had failed to discharge its burden of proving an intention to defraud, dismissed the plaintiff's claim. Thus, the plaintiff appealed. The issues that arose were (i) whether the business of the second defendant had been carried out with intent to defraud its creditors and satisfied the principles of fraudulent trading under s. 304 of the Companies Act 1965 ('CA'); (ii) whether the facts of this instant case justified the lifting of the corporate veil; and (iii) whether the plaintiff was entitled to exemplary damages.

Held (allowing appeal)

Per Hasnah Mohammed Hashim JCA delivering the judgment of the court:

(1) The fact that the incorporation of the third defendant on 4 September 2009 by the first defendant was due to Suit 93 which was commenced on 16 February 2009, could be equated to fraudulent trading as defined under s. 304(2) of the CA. The contemporaneous evidence clearly showed that the third defendant was incorporated prior to CJ, making it possible for the first defendant to have incorporated a company in contemplation of evading payments about one and a half year prior to the CJ. Clearly, the third defendant was incorporated as part of a plan to defraud the plaintiff *vis a vis* the CJ. (paras 27 & 29)

(2) The first defendant had admitted in evidence that the value of the future earnings transferred from the second defendant to the third defendant totalled more than RM2.3 million. The first defendant himself admitted that the third defendant was incorporated to receive assignments of the second defendant's consultancy projects. The resolutions were

subsequently passed naming the third defendant as the benefactor of the second defendant's fees. The consequence of the aforesaid assignment led to the second defendant's business being transferred to the third defendant. The second defendant was now a dormant company. It was thus impossible to conclude that there was no intention to defraud the creditors by the first defendant. There was clear evidence of an intention to defraud by the defendants to evade payments of debts due by the second defendant. (paras 35-37)

(3) The first defendant was the controlling mind of both the second and third defendants. The first defendant was not only a director in the second defendant and held 100% shareholding but also a director in the third defendant with 85% shareholding. The first defendant was also in control of the second defendant. The first defendant gave evidence that the third defendant was in fact incorporated to receive the payments of professional fees for work undertaken by the second defendant. Further, the second defendant's expenses were also borne by the third defendant. It could be reasonably inferred that the two companies had operated as a single commercial entity. The first defendant was clearly the *alter ego* of both the two companies. Thus, the corporate veil ought to be lifted as there was evidence to show a clear intention of the defendants attempting to defraud the plaintiff by depriving it from receiving the sums as agreed in the CJ. The first defendant had carried on the business of the second defendant with intention to defraud the plaintiff, as the second defendant's creditor. (paras 45-48)

(4) Exemplary damages are not intended to compensate the plaintiff and are not recoverable as a matter of right. Thus, applying the principles in *Rookes v. Barnard* to the factual circumstances and evidence of the case, there was absolutely no basis for any exemplary damages, which was punitive in nature, to even be considered. (paras 53 & 54)

Bahasa Malaysia *Headnotes*

Perayu ('plaintif') memulakan tindakan terhadap responden pertama ('defendan pertama') dan responden kedua ('defendan kedua') ('Guaman 93'). Pada waktu material itu, defendan pertama adalah salah satu daripada dua pengarah dan memegang 100% saham dalam syarikat defendan kedua. Satu penghakiman persetujuan ('PP') telah dimasuki antara pihak-pihak. Menurut PP, plaintif, bersama-sama dengan defendan pertama dan defendan kedua, bersetuju untuk menyelesaikan Guaman 93. Fakta-fakta material syarat-syarat PP adalah, antara lain, (i) bahawa defendan pertama dan defendan kedua membayar RM1,150,000 kepada plaintif sebagai penyelesaian penuh dan muktamad ('jumlah penyelesaian'); (ii) bahawa jumlah penyelesaian dibayar secara ansuran; (iii) sekiranya berlaku kegagalan

mematuhi syarat-syarat pembayaran, plaintif harus pertama sekali mengeluarkan notis kepada defendan pertama dan/atau defendan kedua memberikan tempoh lima bulan untuk meremedi kegagalan itu ('notis lima bulan'); dan (iv) sekiranya defendan pertama dan/atau defendan kedua masih gagal meremedikan kegagalan itu, plaintif boleh melaksanakan PP untuk jumlah RM1,450,000 ('jumlah penghakiman penuh'). Defendan pertama dan/atau defendan kedua membayar jumlah RM654,000 menurut terma-terma PP dan ke arah jumlah penyelesaian dibayar sepenuhnya. Seterusnya, defendan kedua melanggar PP apabila gagal membuat bayaran secara ansuran bagi bulan Mac 2013 hingga Jun 2013 seperti yang ditetapkan bawah PP. Plaintif mengeluarkan notis-notis lima bulan itu untuk setiap pelanggaran, yang kesemuanya tamat tempoh tanpa mana-mana kegagalan diremedikan. Jumlah penghakiman penuh tetap tertunggak dan masih terhutang pada plaintif. Plaintif kemudiannya mendapat tahu berkenaan tiga projek perundingan yang telah diberikan oleh defendan kedua kepada PLB-KH Bina Sdn Bhd, Tech-Art Sdn Bhd dan Putrajaya Holdings Sdn Bhd ('ketiga-tiga projek'). Defendan kedua meluluskan tiga resolusi ('resolusi-resolusi') untuk menetapkan semula yuran perundingan yang terhutang kepada defendan kedua untuk ketiga-tiga projek itu kepada syarikat responden ketiga ('defendan ketiga'), yang telah diperbadankan oleh defendan pertama. Plaintif menghujahkan resolusi-resolusi dibuat untuk menipu plaintif sebagai pemiutang bayaran jumlah yang masih terhutang bawah terma-terma PP. Plaintif memulakan tindakan terhadap defendan pertama, defendan kedua dan defendan ketiga menuntut, antara lain, satu pengisytiharan bahawa defendan pertama telah menjalankan perniagaan defendan kedua dengan niat untuk menipu plaintif, sebagai pemiutang defendan kedua. Mahkamah Tinggi, mendapati plaintif gagal melepaskan bebanannya untuk membuktikan niat menipu dan menolak tuntutan plaintif. Oleh itu, plaintif merayu. Isu-isu yang timbul adalah (i) sama ada perniagaan defendan kedua telah dilaksanakan dengan niat untuk menipu pemiutang-pemiutangnya dan memuaskan prinsip-prinsip perniagaan secara fraud bawah s. 304 Akta Syarikat 1965 ('AS'); (ii) sama ada fakta-fakta kes ini menjustifikasikan penyingkapan tabir penubuhan; dan (iii) sama ada plaintif mempunyai hak ganti rugi teladan.

Diputuskan (membenarkan rayuan)
Oleh Hasnah Mohammed Hashim HMR menyampaikan penghakiman mahkamah:

(1) Fakta bahawa penubuhan defendan ketiga pada 4 September 2009 oleh defendan pertama disebabkan oleh Guaman 93 yang dimulakan pada 16 Februari 2009, boleh disamakan dengan perniagaan secara fraud seperti yang ditakrifkan bawah s. 304(2) AS. Keterangan semasa ini jelas menunjukkan defendan ketiga telah ditubuhkan sebelum PP, dan ini memberikan peluang kepada defendan pertama untuk menubuhkan syarikat dalam kontemplasi mengelak bayaran setahun setengah sebelum PP. Jelas sekali defendan ketiga ditubuhkan sebagai sebahagian daripada perancangan untuk menipu plaintif *vis a vis* PP.

(2) Defendan pertama mengakui dalam keterangan bahawa nilai pendapatan masa hadapan yang dipindahkan daripada defendan kedua kepada defendan ketiga berjumlah lebih daripada RM2.3 juta. Defendan pertama mengakui bahawa defendan ketiga ditubuhkan untuk menerima tugasan projek-projek konsultan defendan kedua. Resolusi-resolusi telah diluluskan dengan menamakan defendan ketiga sebagai dermawan yuran defendan kedua. Akibat tugasan itu, perniagaan defendan kedua dipindah kepada defendan ketiga. Defendan kedua kini merupakan syarikat yang tidak aktif. Adalah mustahil untuk menyimpulkan bahawa tiada niat untuk menipu pemiutang-pemiutang oleh defendan pertama. Terdapat keterangan jelas niat defendan-defendan untuk menipu supaya dapat mengelak pembayaran yang dihutang oleh defendan kedua.

(3) Defendan pertama adalah minda yang mengawal defendan kedua dan defendan ketiga. Defendan pertama bukan hanya pengarah defendan kedua dan memegang 100% saham tetapi juga pengarah defendan ketiga dengan memegang 85% saham. Defendan pertama juga mengawal defendan kedua. Defendan pertama memberi keterangan bahawa defendan ketiga ditubuhkan untuk menerima bayaran yuran profesional untuk kerja-kerja yang dibuat defendan kedua. Juga, perbelanjaan defendan kedua juga ditanggung oleh defendan ketiga. Dapat disimpulkan secara munasabah bahawa kedua-dua syarikat itu beroperasi sebagai satu entiti komersial tunggal. Defendan pertama jelasnya adalah *alter ego* kedua-dua syarikat. Oleh itu, tabir penubuhan harus disingkap kerana terdapat keterangan menunjukkan niat jelas defendan-defendan cuba menipu plaintif dengan menafikannya dari menerima jumlah yang dipersetujui dalam PP. Defendan pertama telah menjalankan perniagaan defendan kedua dengan niat untuk menipu plaintif, sebagai pemiutang defendan kedua.

(4) Ganti rugi teladan tidak bertujuan untuk memampas plaintif dan tidak boleh dipulihkan sebagai perkara hak. Oleh itu, mengguna pakai prinsip-prinsip *Rookes v. Barnard* pada fakta-fakta keadaan dan keterangan kes ini, tiada dasar untuk ganti rugi teladan, yang bersifat penghukum, untuk diambil kira.

Case(s) referred to:

Chin Chee Keong v. Toling Corporation (M) Sdn Bhd [2016] 6 CLJ 666 CA ***(refd)***

Faiza Ben Hashem v. Shayif [2008] EWHC 2380 (Fam) ***(refd)***

Gurbachan Singh Bagawan Singh & Ors v. Vellasamy Pennusamy & Other Appeals [2015] 1 CLJ 719 FC ***(refd)***

R v. Grantham [1984] BCLC 270 ***(refd)***

R v. Sinclair [1968] 1 WLR 1246 ***(refd)***

Re Gerald Cooper Chemical Ltd [1978] 2 All ER 49 ***(refd)***

Re William C Leitch Bros Ltd (No 1) [1932] Ch 71 ***(refd)***
Roshairee Abd Wahab v. Mejar Mustafa Omar & Ors [1997] 1 CLJ Supp 39 HC ***(refd)***
Rookes v. Barnard [1964] 1 All ER 367 ***(foll)***
Salomon v. Salomon & Co [1897] AC 22 ***(refd)***
Sambaga Valli K R Ponnusamy v. Datuk Bandar Kuala Lumpur & Ors And Another Appeal [2017] 1 LNS 500 CA ***(refd)***
Sinnaiyah & Sons Sdn Bhd v. Damai Setia Sdn Bhd [2015] 7 CLJ 584 FC ***(refd)***

Legislation referred to:
Companies Act 1965, s. 304(1), (2)

Other source(s) referred to:
Chan & Koh On, *Malaysia Company Law, Principles & Practice,* 2nd edn, Thomson Sweet & Maxwell Asia, p 102

For the appellant - CK Yeoh & Jeffrey Lee; M/s Ranjit Singh & Yeoh
For the respondents - Sandosh Anandan; M/s Sandosh Anandan

[Editor's note: Appeal from High Court, Kuala Lumpur; Civil Suit No: WA-22NCVC-680-11-2016 (overruled).]

Reported by Suhainah Wahiduddin

JUDGMENT

Hasnah Mohammed Hashim JCA:

[1] This is an appeal from a judgment of S Nantha Balan J, sitting in the High Court of Kuala Lumpur, dismissing the appellant's claim after full trial.

[2] We heard the appeal on 11 April 2018. After hearing both counsel for the appellant and the respondent, we accordingly, at the end of the arguments, allowed the appeal with costs of RM45,000 here and below subject to payment of allocator fees. Our reasons for doing so now follow.

[3] For the purpose of the judgment, the parties will be referred to as they were in the High Court.

Brief Facts

[4] The pertinent facts are as follows:

(i) On or about 16 February 2009, the plaintiff commenced an action against the first defendant and second defendant *vide* Kuala Lumpur High Court Civil Summons No: S-22-93-2009 ("Suit 93"). At the material time, the first defendant was one of two directors and held 100% shareholding in the second defendant.

(ii) A consent judgment ("CJ") was entered between the parties on 9 February 2011. Pursuant to the CJ, the plaintiff together with the first defendant and second defendant agreed to settle the Suit 93. The material terms of CJ are as follows:

A (a) The first defendant and second defendant shall pay RM1,150,000 to the plaintiff as full and final settlement ("settlement sum"). The first defendant's liability is discharged after the first RM500,000 is paid.

B (b) The settlement sum is to be paid by instalments in accordance with a schedule set out in the CJ.

(c) In the event of a default on the terms of payment, the plaintiff must first issue a notice to the first defendant and/or the second defendant (whichever is applicable), giving a five months period to remedy the default ("five month notice").

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(d) In the event the first defendant and/or the second defendant still fail to remedy the default, the plaintiff can execute the CJ for the sum of RM1,450,000 ("full judgment sum") together with interest at 5% per annum from the date of default until full realisation, minus the sums already paid under CJ.

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(iii) The first defendant and/or the second defendant paid a total of RM654,000 in accordance with the terms of the CJ and towards satisfaction of the settlement sum. At that stage, the obligation to pay the balance of the settlement sum, ie, RM496,000 was solely on the

E second defendant.

(iv) Subsequently, the second defendant breached the CJ when it failed, refused and/or neglected to pay the instalments for the months of March 2013 to June 2013 as prescribed under the CJ. To this end, the plaintiff issued five month notices in respect of each of these breaches,

F all of which expired without any of the default being remedied.

(v) The full judgment sum of RM796,000 (RM1,450,000 + interest of 5% per annum – the sum already paid by the first defendant/second defendant under the CJ (ie, RM654,000)) remains outstanding and due to the plaintiff.

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(vi) The plaintiff became aware three consultancy projects that the second defendant was engaged with PLB-KH Bina Sdn. Bhd., Tech-Art Sdn. Bhd. and Putrajaya Holdings Sdn. Bhd. ("the three projects"). In 2011, the second defendant passed three resolutions ("the resolutions") to

H reassign the consultancy fees due to the second defendant for the three projects to the third defendant, a company incorporated on 4 September 2009 (of which the first defendant is a director).

(vii) The plaintiff contended that the resolutions were made to defraud the plaintiff as a creditor the payment of the balance sum due under the

I terms of the CJ.

(viii) The plaintiff then initiated an action against first defendant, second defendant and third defendant in Kuala Lumpur High Court on 3 November 2016, seeking the following principal reliefs:

(a) A declaration that the first defendant has carried on the business of the second defendant with intention to defraud the plaintiff, as the second defendant's creditor.

(b) Consequential to prayer (a) above, an order that the first defendant be personally liable to pay the plaintiff the sum of RM796,000 together with interest thereon of 5% per annum from 8 March 2013 until full realisation ("outstanding sum"), being the debt owed by the second defendant to the plaintiff under the judgment.

(c) In the alternative to prayer (b) above, an order that the first and third defendants be jointly and severally liable to pay to the plaintiff the outstanding sum.

(d) Exemplary damages against the first and/or third defendants.

(ix) The second defendant contended that it had only received RM362,980.90 in relation to the payment of fees for the three projects despite that defendants have paid a total sum of RM654,000 to the plaintiff.

(x) On 25 July 2017, learned High Court Judge dismissed the appellant's suit against the defendants. Hence, this appeal before us.

Findings Of The High Court

[5] The learned judge found that the plaintiff had failed to discharge its burden of proving an intention to defraud. The reasoning of the learned judge in reaching the conclusion that he did, may be summarised as follows:

(i) In terms of timelines, it was "too incredulous" and/or "too far-fetched" to suggest that the third defendant's incorporation (which took place about 17 months prior to the recording of the CJ) was done to defraud the plaintiff under the CJ.

(ii) The third defendant only received RM362,980.90 from the second defendant's clients under the consultancy projects, which is clearly less than the amount which was paid under the CJ, ie, RM654,000 and there is no evidence that the third defendant received anything more.

(iii) The first defendant's liability under the CJ was only up to RM500,000. The fact that the plaintiff was paid RM654,000 (ie, beyond RM500,000) does not suggest that there was an intention to defraud the plaintiff.

(iv) In summary, there was every intention on the part of the first defendant/second defendant to pay what was outstanding under the CJ based on the following:

(a) The fact that payments continued to be made after the resolutions were passed, until February 2013;

(b) The fact that first defendant/second defendant paid RM654,000, which was RM154,000 above and beyond the RM500,000 threshold; and

(c) The absence of any evidence to show that the third defendant received anything more than RM362,980.90.

(v) The corporate veil should not be lifted due to lack of evidence to show intention of the defendants attempting to defraud the plaintiff, or to prove that the third defendant received more than RM362,980 from the three assignments.

The Appeal

[6] In the memorandum of appeal, various grounds are raised assailing the impugned decision but before us, learned counsel for the plaintiff focussed his arguments on the following issues:

(a) whether the business of the second defendant has been carried out with intend to defraud its creditors and satisfied the principles of fraudulent trading under s. 304 of Companies Act 1965 (CA 1965");

(b) whether the facts of this instant case justified lifting of the corporate veil, and

(c) whether the plaintiff is entitled to exemplary damages?

Parties' Competing Submissions

[7] The main crux of learned counsel's submission is that the learned judge's inferences and/or conclusion from the evidence were plainly wrong, and that there was insufficient judicial appreciation of the evidence. Learned counsel further submitted that the evidence adduced by the plaintiff at the trial are more than sufficient to prove that there was intention to defraud.

[8] Learned counsel posited that the defendants' intention to defraud was apparent from the following facts:

(a) On 16 February 2009, the plaintiff brought an action against the first defendant/second defendant *via* the Suit 93;

(b) In the face of the Suit 93, the third defendant was incorporated by the first defendant on 4 September 2009;

(c) The CJ was entered on 9 February 2011;

(d) In March and May 2011 (ie, one to three months after the CJ), the resolutions were passed by the first defendant, essentially transferring the second defendant's future income to the third defendant;

(e) By the first defendant's own admission, the value of future income that was transformed from the second defendant to the third defendant totalled over RM2.3 million. There was more than sufficient to have satisfied the CJ in full; and

(f) After paying a total of RM654,000 under the CJ, the second defendant is now incapable of paying anything more.

[9] Learned counsel for the plaintiff argued that the learned judge had misconstrued the plaintiff's case – it was not the plaintiff's case that the incorporation of the third defendant was in itself done to defeat the CJ. The timing of the third defendant's incorporation cannot be considered in isolation.

[10] In conclusion, learned counsel submitted that the crux of the plaintiff's case in that the passing of the resolutions to assign the second defendant's fees to the third defendant (totalling over RM2.3 million) was sufficient evidence to establish intent to defraud.

[11] With regards to the issue of separate legal entities, learned counsel submitted that the learned judge erred in law and in fact in holding that there was no justification to lift the corporate veil. It was the contention of learned counsel for the appellant that the learned judge failed to appreciate that the defendants are in truth and in fact are single commercial unit and is the alter ego and/or controlling mind of the second defendant and/or the third defendant.

[12] In support of his submission, learned counsel took us through the following evidence:

(a) At the material time, the first defendant was one of two directors in the second defendant and held 100% of the shareholding in the second defendant. The first defendant admitted that he is in total control of the second defendant.

(b) The first defendant is also one of two directors in the third defendant and holds 85% of the shareholding in the third defendant. The first defendant agreed that third defendant's projects to the world that the first defendant is the only person behind the ZNA "brand".

(c) Despite the fact that the second defendant and the third defendant are separate entities, the third defendant's website also represents that the business of third defendant is "established since 1992", when this year must in fact refer to the establishment of the first defendant's previous sole proprietorship "Perunding ZNA" ie, a different entity altogether.

(d) The first defendant gave evidence that the third defendant was incorporated to receive the reassignments of the second defendant's fees. These were professional fees for work already done by the second defendant before the CJ was entered. If the separate legal entity principle is observed, there is no justification for the third defendant to receive such fees.

(e) The first defendant testified that the second defendant's expenses are borne by the third defendant and that the third defendant gave money to second defendant to pay off the second defendant's debts.

(f) The five month notices, which were served on the second defendant at its business address, were acknowledged by the third defendant with the third defendant's company stamp, despite the fact that the second defendant (and not the third defendant) was the addressee.

[13] In light of the above, learned counsel for plaintiff submitted that the corporate veil ought to be lifted against the first defendant and/or the third defendant to make them liable to the second defendant's debt under the CJ, as fraud at common law or in equity had been committed against the plaintiff.

[14] With regards to exemplary damages, learned counsel submitted that the circumstances of this instant case falls within the second categories which the exemplary damages may be awarded (See: *Rookes v. Barnard* [1964] 1 All ER 367).

[15] In reply, learned counsel for the defendants submitted that the learned judge was correct in concluding that the plaintiff's claim of fraudulent trading must fail in the absence of sufficient proof. The plaintiff had merely pleaded fraud under fraudulent trading without showing the particulars of fraud nor giving evidence of instances of fraud taking place.

[16] The learned judge was correct in holding that the corporate veil should not be lifted due to lack of evidence to show intention of the defendants attempting to defraud the plaintiff or to prove that the third defendant received more than RM362,980.90 from the three assignments.

[17] Concerning exemplary damages, learned counsel contended that there is no legal basis and evidence to support the plaintiff's claim for the same.

Our Findings

Fraudulent Trading Under Section 304 Of CA 1965

What Constitutes An "Intent To Defraud"

[18] Fraudulent trading is dealt with in sub-s. 304(1) of CA 1965. The subsection provides:

> (1) If in the course of the winding up of a company or in any proceedings against a company it appears that any business of the company has been carried on with intent to defraud creditors of the company or creditors of any other person or for any fraudulent purpose, the Court on the application of the liquidator or any creditor or contributory of the company, may, if it thinks proper so to do declare that any person who was knowingly a party to the carrying on of the business in that manner shall be personally responsible, without any limitation of liability, for all or any of the debts or other liabilities of the company as the Court directs.

[19] In the case of *Chin Chee Keong v. Toling Corporation (M) Sdn. Bhd.* [2016] 6 CLJ 666; [2016] 4 MLRA 180, this court stated:

> [16] The primary object behind subsection 304(1) of the Companies Act 1965 is to statutorily provide for the lifting of the veil of incorporation in the specific circumstances of fraudulent trading with a view to ultimately pinning personal accountability and liability on the directing minds behind such trading of the company. Subsection 304(1) affords the creditor of the company a civil remedy personally against such persons.
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> [17] This court recently had opportunity to consider the operation and ambit of sub-s. 304(1) of the Companies Act 1965 in the case of *Aneka Melor Sdn Bhd v. Seri Sabco (M) Sdn Bhd & Another Appeal* [2016] 2 CLJ 563. His Lordship, Justice Mohd Zawawi Salleh JCA, writing for the court succinctly observed that:
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> > [37] Section 304 of the Companies Act 1965 is aimed principally at curbing the possibility on the part of the officers of a company to act opportunistically and take advantage of the principle of the separate legal personality of a company and the principle of limited liability. As an exception to these principles, there are circumstances when the law duly acknowledges, and for which it accordingly provides the possibility, in very specific situations, for the corporate veil to be pierced. Once the corporate veil has been pierced the creditors of the company whose veil has been pierced may satisfy their claims from the personal assets of the company's shareholders.
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> [18] In another recent decision of *Lama Tile (Timur) Sdn Bhd v. Lim Meng Kwang & Anor* [2015] 3 CLJ 763, the Court of Appeal said:

A [23] Section 304 is a specific statutory provision which allows the corporate veil to be lifted in the limited situations specified. Earlier in this judgment we have underlined that it is applicable in a situation where in the course of proceedings against a company, it appears that the business of the company has been carried on with intent to defraud creditors, a creditor can make an application
B to court to request that the court declare that any person who was knowingly a party to such carrying on of the business of the company, to be personally responsible. The evidence in this appeal shows precisely that. The directors and shareholders of LMK Edaran proposedly and knowingly engaged in a course of conduct to mislead the appellant (by adding the 'S' to the signboard), and
C but by the same token transferred the business of LMK Edaran to SLMK Edaran (previously Southern Taipan Sdn Bhd) to render LMK Edaran a dormant company.".

[20] In broad terms, there are two elements to establishing an application under sub-s. 304(2) of CA 1965. These are:

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(a) that the business of the company has been carried out "with intent to defraud creditors …" or for any fraudulent purpose; and

(b) that the defendant who was knowingly a party to the carrying on of the business in that manner.

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[21] The central element of fraudulent trading is "an intent to defraud" or "fraudulent purpose". The first reported decision to address this issue was *Re William C. Leitch Bros Ltd. (No. 1)* [1932] Ch 71 (Ch D). The Court of Appeal in *R v. Grantham* [1984] BCLC 270 provided clarification by citing Maugham J in *Re Leitch (William C) Bros Ltd* [1932] Ch 71: "In my opinion
F I must hold with regard to the meaning of the phrase "carrying on business with intent to defraud creditors" that if a company continues to carry on business to incur debts at a time when there is to the knowledge of the directors no reasonable prospect of the creditors ever receiving payment of those debts, it is in general a proper inference that the company is carrying
G on business with intent to defraud, …".

[22] The court also considered *R v. Sinclair* [1968] 1 WLR 1246 in which the jury was directed with the following instructions to find "intent to defraud": "It is fraud if it is proved that there was the taking of a risk, which there was no right to take, which would cause detriment or prejudice to
H another. You have to be sure that it was deliberate dishonesty". The court rejected that the defendant had to prove that he knew at the time when debts were incurred that there was no reasonable prospect of creditors ever receiving payment of their debts. It was enough if the defendant realised at the time when the debts were incurred that there was no reason for thinking
I that funds would be available to pay the debt when it would become due or

shortly thereafter. These words import a criterion that is partly subjective and partly objective. Thus, in order to establish dishonesty under sub-s. 304(1) of CA 1965 the court must find that:

(i) According to the ordinary standard of reasonable and honest people what was done was dishonest; and

(ii) That the actor himself must have realised that the act was by those standards dishonest.

[23] In the textbook, *Chan & Koh On Malaysia Company Law, Principles & Practice*, 2nd edn, Thomson Sweet & Maxwell Asia, the learned author stated at p. 102:

> 3.099. The expressions "intent to defraud" and "fraudulent purpose" were considered by KL Rekhraj JC (as he then was) in *H Rosen Engineering BV v. Siow Yoon Keong* and the learned Judicial Commissioner applied the "reasonable expectations of an honest business man" test. It was held in *Eng Iron Works Ltd v. Ting Lin Kiew & Anor t*hat section 304(1) could apply even prior to the winding-up of a company. "Fraud" for the purposes of this section is "actual dishonesty involving, according to current notions of fair trading among commercial men, real moral blame.".

[24] With regard to "knowingly", it appears that the scope of personal liability in sub-s. 304(1) of CA 1965 is not restricted just to directors but anyone who is knowingly party to fraudulent trading. (See: *Re Gerald Cooper Chemical Ltd* [1978] 2 All ER 49).

[25] The standard of proof in sub-s. 304(1) of CA 1965 is on balance of probabilities. The term "it appears" is deployed in the subsection. This clearly denotes that a lower standard of proof is required to establish liability under this provision, ie, on a balance of probabilities. (See: *Sinnaiyah & Sons Sdn Bhd v. Damai Setia Sdn Bhd* [2015] 7 CLJ 584; *Aneka Melor Sdn Bhd v. Seri Sabco (M) Sdn Bhd (supra)*).

[26] We must emphasise that liability depends on the facts of each particular case and that the court has not sought to limit or particularise the different ways and means of dishonest conduct which could fall within the ambit of sub-s. 304(1) of CA 1965. Each case would depend on its facts.

[27] We have carefully scrutinised the whole evidence and we are satisfied that the learned judge erred in concluding that the plaintiff failed to prove fraudulent trading. In our view, the fact that the incorporation of the third defendant was due to the Suit 93 can be equated to fraudulent trading as defined under sub-s. 304(2) of CA 1965. The contemporaneous evidence clearly shows that the third defendant was incorporated prior to CJ, making it possible for the first defendant to have incorporated a company in contemplation of evading payments about one and half year prior to the CJ.

[28] We have noted the oral evidence to support such a conclusion. DW2, Raymond Tan, had explained the idea of incorporation of the third defendant was not mooted by the first defendant but rather that the third defendant was incorporated in order for the first defendant to be able to salvage the first defendant's licence which in turn would allow the first defendant to collect payment as the first defendant would be unable to do without a licence.

[29] Looking at the foregoing facts with unprejudiced eye, it clearly showed that the third defendant was incorporated as part of a plan to defraud the plaintiff *vis-à-vis* the CJ.

[30] It is pertinent to note that the plaintiff had pleaded fraud under fraudulent trading. The learned judge had concluded in holding that the plaintiff's claim of fraudulent trading must surely fail in the absence of such proof. The learned judge said in his grounds of judgment:

> … In any event, it is admitted that the plaintiff was paid a total of RM654,000.00 between March 2011 and February 2013 and this is more than the sum that was received by D3 from D2's clients. **And clearly there are no documents to show that D2's clients had paid monies to D3 in excess of RM654,000.00 and that these monies were not paid to the plaintiff.** Ultimately, the evidential position that obtains is that there is just no evidence that D3 received any monies beyond the total sum of RM362,980.90 from D2's clients. (emphasis added)
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> (See: paragraph 34, page 32, Supplementary ROA).

[31] The defendants had expressly pleaded at para. 18.1 of the statement of defence regarding the difficulty in demanding payment of the second defendant's fees and/or problems with the second defendant's license:

> Defendants further refers to paragraphs 17, 17.1, 17.2, 17.3, 17.4, 17.5, 17.6, 17.7 and 17.8 SOC and assert that the **decision to set up D3 was premised on commercial considerations and internal problems faced by D2 in respect of management of D2.** D2's business and reputation was damaged due to the internal issues which had resulted in the loss of confidence by clients of D2 and not as otherwise contended by the Plaintiff. Defendants shall refer to such evidence during trial. (emphasis added)
>
> (See: paragraphs 18.1. Statement of Defence (page 66 ROA Part [A])).

[32] As we have alluded to earlier in this judgment, in order to attach personal liability to another, the following elements must be fulfilled:

(a) there is an "intent to defraud" in the manner by which the business of the company is being conducted; and

(b) that the person was "knowingly a party" to the carrying on of the business in the fraudulent manner so described.

[33] Therefore, for the plaintiff to be able to successfully sustain a claim for fraud on the part of the respondent, firstly, there must be proof to show that the business of the second defendant had been conducted with intent to defraud its creditors. Secondly, the second defendant must be proven to be a person who was "knowingly a party" to the carrying on of the business in the fraudulent manner however there is no evidence to support either one of the elements listed above.

[34] The basic rule is that he who alleges fraud has the burden of proving them. The court has stressed time and again that allegations must be proven by sufficient evidence because mere allegation is definitely no evidence. Moreover, fraud is not presumed – it must be proved by clear and convincing evidence.

[35] On 16 February 2009 the plaintiff filed an action against the first and second defendants, Suit 93. This was followed with the incorporation of the third defendant and the CJ on 9 February 2011. Sometime between March and May 2011 the resolutions were passed by the first defendant transferring the second defendant's expected future earnings to the third defendant. The first defendant had admitted in evidence that the value of the future earnings transferred from the second defendant to the third defendant totalled more than RM2.3million.The first defendant himself had admitted that the third defendant was in fact incorporated to receive assignments of the second defendant's consultancy projects. The resolutions were subsequently passed naming the third defendant as the benefactor of the second defendant's fees.

[36] The consequence of the aforesaid assignment led to the second defendant's business being transferred to the third defendant. The second defendant is now a dormant company. We are of the view on the facts and evidence of this instant appeal, it is impossible to conclude that there was no intention to defraud the creditors by the first defendant. The resolutions passed had caused monies due and owing to the second defendant in excess of RM2.3million to be assigned to third defendant.

[37] Section 304(1) of the CA 1965 only uses the term "if it appears" which indicates that a lower degree of proof is required. But, even on a higher degree of proof, the result would be the same – that there is clear evidence of an intention to defraud by the defendants to evade payments of debts due by the second defendant.

Lifting Of Corporate Veil

[38] Learned counsel for the plaintiff argued that the first defendant, second defendant and third defendant are in reality a single commercial unit and the first defendant is clearly the alter ego or controlling mind of the second and the third defendant.

[39] One of the fundamental principles of company law is that a company has a personality that is distinct from that its shareholders. This rule enunciated by the House of Lords in *Salomon v. Salomon & Co.* [1897] AC 22 in which it was held that even if one individual held almost all the shares and debentures in a company, and if the remaining shares were held on trust for him, the company is not to be regarded as mere shadow of that individual. Lord MacNaughten stated at p. 51:

> The company is at law a different person altogether from the subscribers to the Memorandum; and, though it may be that after incorporation the business is precisely the same as it was before, and the same persons are managers, and the same hands receive the profits, the company is not in law the agent of the subscribers or trustee for them. Nor are the subscribers as members liable, in any shape or form, except to the extent and in the manner provided by the Act.

[40] A rigid application of the principle, however, may sometimes cause damage to the rights of parties who deal with the corporate because its controllers may be using the corporate structure as a facade to perpetrate wrongdoing.

[41] Thus, there are certain statutory exceptions to the rule in *Salomon* which involve a director being made liable for debts of the company because of breach of the companies or insolvency legislation. This is known as lifting the corporate veil.

[42] Subsection 304(1) of CA 1965 is the statutory exception of the common law position that the corporate veil can be lifted in circumstances where dishonest conduct amounting to fraud at common law or in equity is established on the facts of the case. (See: *Chin Chee Keong v. Toling Corporation (M) Sdn Bhd (supra)*).

[43] In *Faiza Ben Hashem v. Shayif* [2008] EWHC 2380 (Fam), Munby J applied the following principles which are a useful summary of the current state of the law:

(i) Piercing the corporate veil is appropriate only where special circumstances indicated that it is a mere facade.

(ii) Control of a company by the intended defendant is not of itself enough to justify piercing.

(iii) Piercing should not occur merely because it is thought necessary in the interests of justice: there has to be impropriety.

(iv) The impropriety has to be linked to the use of the company structure.

[44] Some shams or facades may be obvious, but many others are not as visible. The courts are reluctant to provide precise guidelines so as to define what constitutes a sham preferring the flexibility of a case by case approach. Useful tests to be employed when trying to identify a sham are:

(i) Are the relevant entities in common ownership?;

(ii) Are the relevant entities in common control?;

(iii) Was the company structure was put in place before or after a particular liability (or serious risk) arose, and if the latter then to what extent was the liability or risk a motivating factor for those who set up the structure?; and

(iv) Was the company structure put in place in an attempt to allow an activity which would be unlawful if carried out personally?

[45] The learned High Court Judge found that there was no justification to lift the corporate veil. With respect, we disagree that there is no justification to pierce the corporate veil. A company is an entity separate from its shareholders and that a subsidiary and its parent or holding company are separate entities having separate existence. On the facts and evidence it can be concluded that the first defendant is the controlling mind of both the second and third defendants.

[46] The first defendant was not only a director in the second defendant and held 100% shareholding but also a director in the third defendant with 85% shareholding. He admitted in evidence that he is in total control of the second defendant. The first defendant gave evidence that the third defendant was in fact incorporated to receive the payments of professional fees for work undertaken by the second defendant. Further, the second defendant's expenses were also borne by the third defendant.

[47] In the appeal before us, it could be reasonably inferred that the two companies had operated as a single commercial entity. The first defendant is clearly the *alter ego* of both the two companies. The Federal Court in the case of *Gurbachan Singh Bagawan Singh & Ors v. Vellasamy Pennusamy & Other Appeals* [2015] 1 CLJ 719 held:

> [96] But in the event that we should, we are of the view that it is now a settled law in Malaysia that the court would lift the corporate veil of a corporation if such corporation was set up for fraudulent purposes, or where it was established to avoid an existing obligation or even to prevent the abuse of a corporate legal personality.
>
> [97] As to what constitutes fraudulent purposes, it has been described as to include actual fraud or fraud in equity. And fraud in equity occurred in '... cases where there are signs of separate personalities of companies being used to enable persons to evade their contractual obligations or duties, the court would disregard the notional separateness of the companies ...

[48] We are of the view that the corporate veil ought to be lifted as there are evidence to show a clear intention of the defendants attempting to defraud the plaintiff by depriving it from receiving the sums as agreed in the CJ. We find that the first defendant has carried on the business of the second defendant with intention to defraud the plaintiff, as the second defendant's creditor.

Exemplary Damages

[49] The concept of exemplary damages has been explained by this court in *Sambaga Valli K R Ponnusamy v. Datuk Bandar Kuala Lumpur & Ors and Another Appeal* [2017] 1 LNS 500; [2018] 1 MLJ 784:

> [33] The exemplary damages or punitive damages – the two terms now regarded as interchangeable – are additional damages awarded with reference to the conduct of the defendant, to signify disapproval, condemnation or denunciation of the defendant's tortious act, and to punish the defendant. Exemplary damages may be awarded where the defendant has acted with vindictiveness or malice, or where he has acted with a "contumelious disregard" for the right to the plaintiff. The primary purpose of an award of exemplary damages may be deterrent, or punitive and retributory, and the award may also have an important function in vindicating the rights of the plaintiff. (See *Rookes v. Barnard* [1964] 1 All ER 347; *A B v. Southwest Water Services* [1993] All ER 609 *Broome v. Cassell & Co* [1971] 2 QB 354, *Laksamana Realty Sdn. Bhd. v. Goh Eng Hwa and Another Appeal* [2005] 4 CLJ 871; [2006] 1 MLJ 675).

[50] There are two categories provided in the case of *Rookes v. Barnard (supra)*, for claim of exemplary damages:

> … The first category is oppressive, arbitrary or unconstitutional action by the servants of the government. I should not extend this category – I say this with particular reference to the facts of this case – to oppressive action by private corporations or individuals. Cases in second category are those in which the defendant's conduct has been calculated by him to make a profit for himself which may well exceed the compensation payable to the plaintiff … .

[51] In this instant appeal, the plaintiff sought exemplary damages. In claiming exemplary damages under the second category, the plaintiff must be able to prove that the defendants have made a profit for themselves.

[52] James Foong J (as he then was) in *Roshairee Abd. Wahab v. Mejar Mustafa Omar & Ors* [1997] 1 CLJ Supp 39 had set the guidelines for awarding exemplary damages:

> While considering the request for exemplary damages, this Court must bear in mind that the objective for an award under this category is to punish the defendants, and to display the Court's indignant attitude towards the acts committed by the defendants. However, from the enlightening judgment of Lord Devlin in *Rookes v. Bernard* [1946] AC 1129, such damages must be restricted to situations where there are:

> "... oppressive, arbitrary or unconstitutional action by the servants of the Government" or where "the defendant's conduct has been calculated by him to make a profit for himself which may well exceed the compensation payable to the plaintiff."
>
> Outside these 2 categories, exemplary damages should not be awarded.

[53] This court in *Sambaga Valli KR Ponnusamy (supra)* explained with clarity that exemplary damages are not intended to compensate the plaintiff and are not recoverable as a matter of right:

> … we would like to emphasise again that exemplary damages are not intended to compensate the plaintiff and are not recoverable as a matter of right. The amount of the exemplary damages award is left to the judge's discretion and is determined by considering the character of the defendant's misconduct, the nature and extension of the plaintiff's injury and the means of the defendant. The quantum of exemplary damages to be awarded must be appropriate to the wrongdoing inflicted to the parties involved. Exemplary damages must not be uncontrolled or arbitrary; they must be of an amount that is the minimum necessary to achieve their purpose in the context of the particular case.

[54] Thus, applying the principles in *Rookes v. Barnard (supra)* to the factual circumstances and evidence of the case, there is absolutely no basis for any exemplary damages, which is punitive in nature, to be even considered under any of the three categories.

Conclusion

[55] In conclusion, after having heard the parties at length and upon careful perusal of the records of appeals, we are of the considered opinion that this is a case in which appellate intervention is warranted. For the foregoing reasons, we unanimously allowed the appeal with costs of RM45,000 subject to the payment of allocator fees.

[56] The decision of the learned judge is therefore set aside. We ordered that the first and third defendants be jointly and severally liable to pay to the plaintiff the sum RM796,000 together with interest thereon of 5% per annum from 8 March 2013 until full realisation being the debt owed by the second defendant to the plaintiff under the judgment.

[57] We further ordered that the deposit be refunded.